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No. 93-1001

In The Supreme Court of the United States

October Term, 1993

Allied-Bruce Terminix Companies, Inc., and Terminix International Company,
Petitioners,

v.

G. Michael Dobson, Wanda C. Dobson, Steven Gwin and Jan Gwin,
Respondents.

On Writ of Certiorari to the Supreme Court of Alabama

BRIEF FOR PETITIONERS

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QUESTION PRESENTED

Section 2 of the Federal Arbitration Act, 9 U.S.C. § 2, makes an agreement to arbitrate enforceable, as a matter of federal law, provided that it is part of "a contract evidencing a transaction involving commerce." The question presented here is whether Section 2 is inapplicable to contracts otherwise involving interstate commerce if the parties did not "contemplate[] substantial interstate activity" at the time of the contract.

TABLE OF CONTENTS

	Page
QUESTION PRESENTED	i
TABLE OF AUTHORITIES	iv
OPINIONS BELOW	1
JURISDICTION	1
STATUTORY PROVISIONS INVOLVED	2
STATEMENT	2
SUMMARY OF ARGUMENT	6
ARGUMENT	9
I. SECTION 2 APPLIES TO WRITTEN ARBITRATION AGREEMENTS TO THE FULL EXTENT OF LEGISLATIVE POWER UNDER THE COMMERCE CLAUSE	11
II. SECTION 2 CANNOT BE READ, IN ANY EVENT, TO REQUIRE THAT THE PARTIES CONTEMPLATE SUBSTANTIAL INTERSTATE ACTIVITY	23
CONCLUSION	28

TABLE OF AUTHORITIES

CASES

	Page
Agostini Bros. Bldg. Corp. v. United States, 142 F.2d 854 (4th Cir. 1944)	16
American Express Co. v. Iowa, 196 U.S. 133 (1905)	12
American Airlines, Inc. v. Louisville & Jefferson County Air Bd., 269 F.2d 811 (6th Cir. 1959)	22
Bernhardt v. Polygraphic Co. of America, 350 U.S. 198 (1956)	8, 20, 21
Board of Trade v. Olsen, 262 U.S. 1 (1923)	12
Board of Trade v. SEC, 677 F.2d 1137 (7th Cir.), *vacated as moot*, 459 U.S. 1026 (1982)	14
Burke County Pub. Schools Bd. of Educ. v. Shaver Partnership, 279 S.E.2d 816 (N.C. 1981)	23
Dean Witter Reynolds, Inc. v. Byrd, 470 U.S. 213 (1985)	7, 9, 11, 19
Del E. Webb Constr. v. Richardson Hosp. Auth., 823 F.2d 145 (5th Cir. 1987)	8, 21, 22
First Investors Corp. v. American Capital Financial Servs., Inc., 823 F.2d 307 (9th Cir. 1987)	22
Foster v. Turley, 808 F.2d 38 (10th Cir. 1986)	8, 21, 22
Fry v. United States, 421 U.S. 542 (1975)	13
Gibbons v. Ogden, 22 U.S. (9 Wheat) 1 (1824)	12
Gilmer v. Interstate/Johnson Lane Corp., 111 S. Ct. 1647 (1991)	*passim*
Gulf Oil Corp. v. Copp Paving Co., 419 U.S. 186 (1974)	15
Hodel v. Virginia Surface Mining & Reclamation Ass'n, 452 U.S. 264 (1981)	12
Lacheney v. Profitkey Int'l, Inc., 818 F. Supp. 922 (E.D. Va. 1933)	23
Loche v. Dean Witter Reynolds, Inc., 526 N.E.2d 1296 (Mass. App. Ct. 1988)	23
Lopez v. Home Buyers Warranty Corp., 628 So. 2d 361 (Ala. 1993), *reh'g denied*, 1993 Ala. LEXIS 1512 (Sept. 24, 1993), *petition for cert. filed*, 62 U.S.L.W. 3430 (Dec. 22, 1993) (No. 93-995)	8, 26
Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Ware, 414 U.S. 117 (1973)	20

TABLE OF AUTHORITIES—Continued

	Page
Mesa Operating Ltd. Partnership v. Louisiana Interstate Gas Corp., 797 F.2d 238 (5th Cir. 1986)	22
Metro Indus. Painting Corp. v. Terminal Constr. Co., 287 F.2d 382 (2d Cir.), *cert. denied*, 368 U.S. 817 (1961)	*passim*
Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc., 473 U.S. 614 (1985)	9, 17, 18, 26
Moses H. Cone Memorial Hosp. v. Mercury Constr. Co., 460 U.S. 1 (1983)	*passim*
Old Republic Ins. Co. v. Lanier, No. 1921387, 1994 Ala. LEXIS 276 (Ala. Apr. 29, 1994)	26
Pathman Constr. Co. v. Knox County Hosp. Ass'n, 326 N.E.2d 844 (Ind. Ct. App. 1975)	23
Perez v. United States, 402 U.S. 146, 150 (1971)	12
Perry v. Thomas, 482 U.S. 483 (1987)	*passim*
Prima Paint Corp. v. Flood & Conklin Mfg. Co., 388 U.S. 395 (1967)	*passim*
R.J. Palmer Constr. Co. v. Wichita Band Instrument Co., 642 P.2d 127 (Kan. Ct. App. 1982)	23
Robert Lawrence Co. v. Devonshire Fabrics, Inc., 271 F.2d 402 (2d Cir. 1959), *cert. granted*, 362 U.S. 909, *cert. dismissed*, 364 U.S. 801 (1960)	8, 22
Scherk v. Alberto-Culver Co., 417 U.S. 506 (1974)	11
Shearson/American Express, Inc. v. McMahon, 482 U.S. 220 (1987)	17
Snyder v. Smith, 736 F.2d 409 (7th Cir.), *cert. denied*, 469 U.S. 1037 (1984)	21
Societe Generale de Surveillance, S.A. v. Raytheon European Management & Sys. Co., 643 F.2d 863 (1st Cir. 1981)	21, 22
Southland Corp. v. Keating, 465 U.S. 1 (1984)	*passim*
Stafford v. Wallace, 258 U.S. 495 (1922)	12
United States v. Feola, 420 U.S. 671 (1975)	24
United States v. James, 834 F.2d 92 (4th Cir. 1987)	14
United States v. Luskey, 262 U.S. 62 (1923)	14
United States v. Yermian, 468 U.S. 63 (1984)	24

TABLE OF AUTHORITIES—Continued

	Page
Wickard v. Filburn, 317 U.S. 111 (1942)	13
Woermann Constr. Co. v. Southwestern Bell Tel. Co., 846 S.W.2d 790 (Mo. Ct. App. 1993)	22
STATUTES	
Federal Arbitration Act	
§ 1, 9 U.S.C. § 1	*passim*
§ 2, 9 U.S.C. § 2	*passim*
Pub. L. No. 68-401, 43 Stat. 883 (1925)	16
Act of April 19, 1920, ch. 275, 1920 N.Y. Laws 803	16
Ala. Code 1975, § 8-1-41	5
LEGISLATIVE MATERIALS	
H.R. 646, 68th Cong., 1st Sess. (1924)	15
S. 1005, 68th Cong., 1st Sess. (1923)	15
S. 4214, 67th Cong., 4th Sess. (1922)	16
H.R. Rep. No. 96, 68th Cong., 1st Sess. (1924)	*passim*
S. Rep. No. 536, 68th Cong., 1st Sess. (1924)	12
Joint Hearings on S. 1005 & H.R. 646 Before the Subcomm. of the Comms. on the Judiciary, 68th Cong., 1st Sess. (1924)	13
Hearing on S. 4213 & S. 4214 Before a Subcomm. of the Comm. on the Judiciary, 67th Cong., 4th Sess. (1923)	20
65 Cong. Rec. 1931 (1924)	14
OTHER MATERIAL	
The American Heritage Dictionary of the English Language (3d ed. 1992)	7, 14

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BRIEF FOR PETITIONERS

OPINIONS BELOW

The opinion of the Supreme Court of Alabama is reported at 628 So. 2d 354. It is reprinted in the Joint Appendix at 97-103. The order of the circuit court is not reported. It is reprinted in the Joint Appendix at 96.

JURISDICTION

The judgment of the Supreme Court of Alabama was entered on August 13, 1993. A timely petition for rehearing was denied on September 24, 1993. The jurisdiction of this Court is invoked pursuant to 28 U.S.C. § 1257(3). This Court granted the petition for a writ of certiorari on March 21, 1994.

STATUTORY PROVISIONS INVOLVED

Section 2 of the Federal Arbitration Act, 9 U.S.C. § 2, provides:

> **Validity, irrevocability, and enforcement of agreements to arbitrate**
>
> A written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.

Section 1 of the Federal Arbitration Act, 9 U.S.C. § 1, provides in relevant part:

> **"Maritime transactions" and "commerce" defined; exceptions to operation of title**
>
> . . . "commerce", as herein defined, means commerce among the several States or with foreign nations, or in any Territory of the United States or in the District of Columbia, or between any such Territory and another, or between any such Territory and any State or foreign nation, or between the District of Columbia and any State or Territory or foreign nation, but nothing herein contained shall apply to contracts of employment of seamen, railroad employees, or any other class of workers engaged in foreign or interstate commerce.

STATEMENT

This case involves the construction of Section 2 of the Federal Arbitration Act (the "FAA" or "the Act"), 9 U.S.C. § 2.[1] Section 2, as a matter of federal substantive

[1] All parties in the court below are reflected in the caption. The only corporate petitioner in this case—Allied-Bruce Terminix Cos., Inc.—has no parent company or subsidiaries.

law, requires enforcement of arbitration agreements in any "contract evidencing a transaction involving commerce." Section 1 of the Act defines commerce to include "commerce among the several States" (9 U.S.C. § 1). The Alabama Supreme Court refused to enforce the arbitration agreement in this case, however, on the ground that, notwithstanding any *actual* nexus with interstate commerce, the parties had not "*contemplated* substantial interstate activity." J.A. 100 (quoting *Metro Indus. Painting Corp. v. Terminal Constr. Co.*, 287 F.2d 382, 387 (2d Cir.), *cert. denied*, 368 U.S. 817 (1961) (Lumbard, J., concurring)).

The issue in this case arose out of an agreement between Steven and Jan Gwin and petitioners Allied-Bruce Terminix Companies, Inc. ("Terminix Service") and Terminix International Company ("Terminix International").[2] The Gwins, residents of Fairhope, Alabama, had previously agreed to a termite protection plan with a local company, but, upon its expiration, they decided "to go with a national company like Termin[i]x." J.A. 37. Terminix Service is an Arkansas company with offices in Florida, Georgia, Mississippi, Louisiana, Arkansas, Oklahoma, and Texas, as well as in Alabama. J.A. 71-72. Terminix International is a limited partnership with its principal place of business in Memphis, Tennessee. J.A. 79.

The termite protection plan provided for services to be performed by Terminix Service. Terminix International, in turn, guaranteed the terms of the plan. J.A. 80. The contract embodying the plan expressly provided that "any controversy or claim between [the parties] arising out of or relating to the interpretation, performance or breach of any provision of this agreement *shall be settled exclu-*

[2] As we discuss, the contract was later transferred to respondents Michael and Wanda Dobson pursuant to a contract for purchase of the Gwins' home. *See* page 4 *infra*.

sively by arbitration." J.A. 77-78, 79-80 (emphasis added).[3]

The termite protection plan was subsequently transferred to the Dobsons as part of their agreement to purchase the Gwins' home. J.A. 65-66.[4] In addition, Terminix Service performed a visual inspection of the home, as called for in the sales agreement, to check for active infestation. J.A. 38-39, 62-63. Both the termite protection plan and the written report on the visual inspection were presented to the Dobsons at the closing of the sale. J.A. 62-63, 69-70.

Shortly after the closing, in the course of remodeling the home, the Dobsons discovered termites. Petitioners then provided repairs and further treatment, in accordance with the terms of the termite protection plan. Much of the material and equipment used by petitioners to treat the home—specifically including the chemical used to

[3] The full text of the arbitration provision is as follows:

> The Purchaser and Terminix agree that any controversy or claim between them arising out of or relating to the interpretation, performance or breach of any provision of this agreement shall be settled exclusively by arbitration. Such arbitration shall be conducted in accordance with the Commercial Arbitration Rules then in force of the American Arbitration Association before three arbitrators appointed by the American Arbitration Association. The arbitration award shall be final and binding on both parties. Judgment upon such arbitration award may be entered in any court having jurisdiction.

J.A. 78.

[4] The sales agreement included the following provision:

> SELLER IS TO FURNISH WRITTEN EVIDENCE from a bonded and licensed termite control company that a visual inspection by them indicates the dwelling is free from infestation by wood destroying insects and damage caused by currently active infestation. OLD DAMAGE IS NOT CONSIDERED. The current termite contract, if any, is to be transferred to Buyer at Buyer's expense.

J.A. 66.

eliminate and prevent termites—was purchased outside of Alabama and brought into Alabama for use on the home. J.A. 71-72.

The Dobsons, however, remained dissatisfied. Rather than submit their complaints to arbitration, they elected to bring suit against petitioners in Alabama Circuit Court. After amendment of their original complaint, they ultimately asserted claims that petitioners had breached their duties under the termite protection plan, that they had negligently performed the visual inspection, and that they had misrepresented the results of the visual inspection.

Relying on the arbitration clause in the termite protection plan, petitioners sought to obtain a stay of the litigation and an order compelling arbitration. In so doing, petitioners specifically relied upon Section 2 of the Federal Arbitration Act. Petitioners argued that, as a matter of federal law, Section 2 required enforcement of voluntary arbitration agreements and that it preempted contrary state law. Without providing any reason, the Alabama Circuit Court, in a summary order, denied petitioners' motion. J.A. 96.

The Alabama Supreme Court, likewise, refused to enforce the written arbitration agreement. The court first noted that "[p]redispute arbitration agreements are unenforceable under Alabama law." J.A. 98 (citing Ala. Code 1975, § 8-1-41). The court acknowledged that Section 2 of the Federal Arbitration Act required enforcement of arbitration agreements as a matter of federal law, J.A. 98-99, but it held that Section 2 did not apply to this case because the required nexus with interstate commerce was absent. The court rejected petitioners' contention that the scope of Section 2—as reflected in the phrase "contract evidencing a transaction involving commerce"—should be broadly construed as "coextensive with [Congress'] commerce power." J.A. 99. Rather, the court opted to apply a more restrictive standard, stating that " '[t]he significant question, therefore [in determining

whether a contract evidences a transaction involving commerce] is not whether, in carrying out the terms of the contract, the parties *did* cross state lines, but whether, at the time they entered into it and accepted the arbitration clause, they *contemplated* substantial interstate activity.'" J.A. 100 (quoting *Metro Indus.*, 287 F.2d at 387 (Lumbard, J., concurring)).

Applying that test, the court determined that federal law did not apply. The court recognized that performance under the contract "involve[d] interstate commerce" but held that it did not do so "to such a degree that the parties upon entering the contract must have contemplated substantial interstate activity." J.A. 103. Pursuant to the state policy against enforcement of pre-dispute arbitration agreements, therefore, it declined to enforce the agreement.

SUMMARY OF ARGUMENT

Section 2 of the Federal Arbitration Act—enacted pursuant to the "comprehensive powers" of the Commerce Clause (*Southland Corp. v. Keating*, 465 U.S. 1, 15 (1984)—makes "valid, irrevocable, and enforceable" all written arbitration agreements in "a contract evidencing a transaction involving commerce . . . ." 9 U.S.C. § 2. Although this provision embodies "a liberal federal policy favoring arbitration agreements, notwithstanding any state substantive or procedural policies to the contrary," *Moses H. Cone Memorial Hosp. v. Mercury Constr. Co.*, 460 U.S. 1, 24 (1983), the Alabama Supreme Court gave it a narrow reading, holding that it applied only when the parties to a contract "*contemplated* substantial interstate activity." J.A. 100 (internal quotes omitted). This reading, however, is simply incorrect. Rather, as its language and policies demonstrate, "the Federal Arbitration Act . . . embodies Congress' intent to provide for the enforcement of arbitration agreements within the full reach of the Commerce Clause." *Perry v. Thomas*, 482 U.S. 483, 490 (1987).

1. The language of Section 2—the "primary substantive provision of the Act" (*Moses H. Cone*, 460 U.S. at 24)—indicates that Congress intended to exercise its commerce power broadly. Rather than limit the Act to transactions "in" commerce, Congress extended its reach to transactions "involving" commerce, a term that is properly used to mean "influenc[ing]" or "affect[ing]". *See The American Heritage Dictionary of the English Language* 950 (3d ed. 1992). Furthermore, the definition of "commerce," set forth in Section 1 of the Act (9 U.S.C. § 1), directly tracks the words used to define the commerce power ("commerce among the States") granted to Congress under Article I. And, while Section 2 provides that there must be a "contract evidencing" the transaction involving commerce, that language requires only that the contract be "evidence" of the transaction, not of the "commerce." The natural reading of Sections 1 and 2 of the Act, therefore, is that they mandate enforcement of arbitration agreements within the field over which Congress has constitutional power.

That reading of Section 2 is also most consistent with the "federal policy favoring arbitration." *Gilmer v. Interstate/Johnson Lane Corp.*, 111 S. Ct. 1647, 1652 (1991). This Court has often recognized that questions regarding the arbitrability of claims "must be addressed with a healthy regard for the federal policy favoring arbitration," *see Moses H. Cone*, 460 U.S. at 24, and the same regard should be applied to construction of the Act itself. Given its purpose of "ensur[ing] judicial enforcement of privately made agreements to arbitrate," *Dean Witter Reynolds, Inc. v. Byrd*, 470 U.S. 213, 219 (1985), it is highly unlikely that Congress would intentionally have left part of the field open for state policies hostile to arbitration agreements. *See Southland Corp.*, 465 U.S. at 14. And it is equally unlikely that Congress, in seeking to advance an alternative to litigation, would have defined the scope of the Act in a way that promotes ancillary litigation about the applicability of federal law and introduces fur-

ther uncertainty about the validity of private agreements to arbitrate.

Prior decisions of this Court, likewise, suggest that Congress, in enacting Section 2, exercised its commerce power fully. The statement in *Perry* to that effect (*see* page 6 *supra*) merely reflects earlier indications that Section 2 reaches "activity that affected commerce," *Bernhardt v. Polygraphic Co. of America*, 350 U.S. 198, 201 (1956), or "contracts relating to interstate commerce." *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395, 401 n.7 (1967) (quoting H.R. Rep. No. 96, 68th Cong., 1st Sess. 1 (1924)). The same broad interpretation of Section 2 is reflected in decisions of numerous federal courts of appeals. *See, e.g., Robert Lawrence Co. v. Devonshire Fabrics, Inc.*, 271 F.2d 402 (2d Cir. 1959), *cert. granted*, 362 U.S. 909, *cert. dismissed*, 364 U.S. 801 (1960); *Foster v. Turley*, 808 F.2d 38 (10th Cir. 1986); *Del E. Webb Constr. v. Richardson Hosp. Auth.*, 823 F.2d 145 (5th Cir. 1987).

2. Even if Section 2 were read to exercise less than the full commerce power, it could not be read to apply only when the parties to a contract "*contemplate* substantial interstate activity." That test, adopted from a concurring opinion by Judge Lumbard some thirty years ago, simply has no grounding in the Act. The language of the Act plainly calls for an objective, not a subjective, inquiry into the nature of the transaction—*i.e.*, whether it "involv[es] commerce"—and the opinion of Judge Lumbard gives no good reason for thinking otherwise. Thus, although the parties must subjectively agree *to arbitrate*, the scope of federal law does not further depend on what they contemplate about the interstate elements of the transaction.

The Alabama Supreme Court has stated that the "contemplation-of-the-parties" test "better promotes [its] strong public policy against the use of predispute arbitration agreements." *Lopez v. Home Buyers Warranty Corp.*, 628 So. 2d 361, 363 n.2 (Ala. 1993), *reh'g denied*, 1993

Ala. LEXIS 1512 (Sept. 24, 1993), *petition for cert. filed*, 62 U.S.L.W. 3430 (Dec. 22, 1993) (No. 93-995). But a hostility towards arbitration agreements is not a basis for giving a narrow reading to a federal law designed to displace that hostility. Of course, to the extent that the court below is concerned about the fairness of contracts containing arbitration agreements, Section 2, by its terms, allows for invalidation of agreements to arbitrate "upon such grounds as exist at law or in equity for the revocation of *any* contract." 9 U.S.C. § 2 (emphasis added); *see Gilmer*, 111 S. Ct. at 1655-56. What courts may not do, however, is to apply discriminatory state-law principles "that take[] [their] meaning precisely from the fact that a contract to arbitrate is at issue . . . ." *Perry*, 482 U.S. at 492 n.9. That is just what the court below has done here, and its action is invalid as a matter of federal law.

ARGUMENT

Section 2 of the Federal Arbitration Act "is a congressional declaration of a liberal federal policy favoring arbitration agreements, notwithstanding any state substantive or procedural policies to the contrary." *Moses H. Cone Memorial Hosp. v. Mercury Constr. Co.*, 460 U.S. 1, 24 (1983); *see Perry v. Thomas*, 482 U.S. 483, 489 (1987). Drawing upon its "comprehensive powers" under the Commerce Clause, *Southland Corp. v. Keating*, 465 U.S. 1, 15 (1984), Congress "create[d] a body of federal substantive law of arbitrability, applicable to any arbitration agreement within the coverage of the Act." *Moses H. Cone*, 460 U.S. at 24. Within the fields that it encompasses—"maritime transaction[s]" and "transaction[s] involving commerce"—Section 2 requires that courts "rigorously enforce agreements to arbitrate." *Dean Witter Reynolds, Inc. v. Byrd*, 470 U.S. 213, 221 (1985); *see Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 626 (1985). That obligation is binding on both federal and state courts. *See Southland Corp.*, 465 U.S. at 15.

The Alabama Supreme Court nevertheless held that it was free to deny enforcement of the arbitration agreement in this case, finding that federal law was inapplicable. The court reached this result by concluding that, whatever the actual nexus with interstate commerce, a transaction does not "involv[e] commerce" within the meaning of Section 2 unless "at the time they entered into [the contract] and accepted the arbitration clause, [the parties] *contemplated* substantial interstate activity." J.A. 100 (quoting *Metro Indus. Painting Corp. v. Terminal Constr. Co.*, 287 F.2d 382, 387 (2d Cir.), *cert. denied*, 368 U.S. 817 (1961) (Lumbard, J., concurring) (*Metro Indus.*). Thus, even though the parties here had agreed to arbitrate all disputes arising out of the transaction, and even though the transaction involved parties in different states and materials shipped across state lines, the federal policy favoring enforcement of arbitration agreements was disregarded. In its place, the court applied state law *barring* enforcement of predispute arbitration agreements.

This reading of Section 2 is simply indefensible. To arrive at it, the court below necessarily accepted two propositions with respect to congressional intent: first, that Congress, in exercising its power over interstate commerce, meant to use only a fraction of that power and, second, that, in doing so, Congress further intended to make the parties' subjective views *about the extent of interstate commerce* into the touchstone of Section 2 application. Both propositions are incorrect. The language and policies of the Act demonstrate that Congress wanted to override legislative and judicial hostility to arbitration agreements to the full extent of its powers and that, in any event, it is the actual nexus of transactions to interstate commerce, not the subjective views of the contracting parties, that defines the jurisdictional reach of Section 2.

I. SECTION 2 APPLIES TO WRITTEN ARBITRATION AGREEMENTS TO THE FULL EXTENT OF LEGISLATIVE POWER UNDER THE COMMERCE CLAUSE

The purpose of the Federal Arbitration Act, originally enacted in 1925, was "to ensure judicial enforcement of privately made agreements to arbitrate." *Dean Witter Reynolds*, 470 U.S. at 219; *see Gilmer v. Interstate/Johnson Lane Corp.*, 111 S. Ct. 1647, 1651 (1991); *Scherk v. Alberto-Culver Co.*, 417 U.S. 506, 510 n.4 (1974). As this Court has stated, "[t]he problems Congress faced were . . . twofold: the old common-law hostility toward arbitration, and the failure of state arbitration statutes to mandate enforcement of arbitration agreements." *Southland Corp.*, 465 U.S. at 14. The Act sought "to place an arbitration agreement 'upon the same footing as other contracts, where it belongs.'" *Dean Witter Reynolds*, 470 U.S. at 219 (quoting H.R. Rep. No. 96, 68th Cong., 1st Sess. 1 (1924)).

The "primary substantive provision of the Act" (*Moses H. Cone*, 460 U.S. at 24) is Section 2, which provides that arbitration agreements "shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract." To be within the scope of the Act, however, an arbitration provision must meet two conditions: first, it must be written and, second, it must be "in any maritime transaction or a contract evidencing a transaction involving commerce." Section 1 of the Act defines the term "commerce" to "mean[] commerce among the several States or with foreign nations . . . ."

The reference to "transactions involving commerce" in Section 2 indicates what this Court has repeatedly recognized: that, in enacting Section 2, Congress was relying upon its powers under the Commerce Clause. *See Perry*, 482 U.S. at 491 & n.8; *Southland Corp.*, 465 U.S. at 14-15; *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388

U.S. 395, 405 (1967). That much was settled (after some debate) by the decision in *Prima Paint*, where the Court expressly held that "the federal arbitration statute is based upon and confined to the incontestable federal foundations of 'control over interstate commerce and over admiralty.'" 388 U.S. at 405 (quoting H.R. Rep. No. 96, 68th Cong., 1st Sess. 1 (1924)); S. Rep. No. 536, 68th Cong., 1st Sess. 3 (1924). Later, in holding that Section 2 of the Act applies in state as well as federal courts, the Court emphasized the fact that Congress had "draw[n] on the comprehensive powers of the Commerce Clause." *Southland Corp.*, 465 U.S. at 15.

Given the breadth of these "comprehensive powers," there seems little doubt that, so long as Congress exercised them to the fullest, the arbitration agreement in this case is enforceable as a matter of federal law. One hundred years before passage of the Act, this Court stated that the federal power over interstate commerce is "complete in itself, may be exercised to its utmost extent, and acknowledges no limitations other than are prescribed in the constitution." *Gibbons v. Ogden*, 22 U.S. (9 Wheat.) 1, 196 (1824); *see also Hodel v. Virginia Surface Mining & Reclamation Ass'n*, 452 U.S. 264, 276 (1981) ("the Commerce Clause is a grant of plenary authority to Congress."). And, it is now accepted that the power over commerce "extends not only to 'the use of channels of interstate or foreign commerce' and to 'protection of the instrumentalities of interstate commerce . . . or persons or things in commerce,' but also to 'activities affecting commerce.'" 452 U.S. at 276-77 (quoting *Perez v. United States*, 402 U.S. 146, 150 (1971)).[5] Thus, "[e]ven

[5] Although the boundaries of the Commerce Clause have been subject to varying definitions over the years, decisions prior to passage of the Act had indicated that its scope extended at least to contracts "concerning interstate commerce" (*American Express Co. v. Iowa*, 196 U.S. 133, 143 (1905)) or to intrastate activities "burden[ing]" interstate commerce. *Board of Trade v. Olsen*, 262 U.S. 1, 36 (1923). *See also Stafford v. Wallace*, 258 U.S. 495, 521 (1922). Indeed, a brief submitted to Congress in 1924, by Julius H. Cohen, a member of the Committee on Commerce, Trade & Commercial Law of the ABA and General Counsel for the N.Y. State Chamber of Commerce, stated that "[i]t is not only the actual and physical interstate shipment of goods which is subject to the interstate commerce powers of the Federal Government, but these powers govern every agency or act which bears so close a relationship to interstate commerce that they can reasonably be said to affect it. Contracts relating to interstate commerce are within the regulatory powers of Congress. (*Board of Trade v. Olsen*, U.S.S.C. Adv. Op. No. 13, May 1, 1923, p. 519; *American Express Co. v. Iowa*, 196 U.S. 133, 143.)" Joint Hearings on S. 1005 & H.R. 646 Before the Subcomm. of the Comms. on the Judiciary, 68th Cong., 1st Sess. 38 (1924). The House Report subsequently used the same language ("contracts relating to interstate commerce") in describing the scope of the powers granted by the Commerce Clause. *See* page 14 *infra*.

activity that is purely intrastate in character may be regulated by Congress, where the activity, combined with like conduct by others similarly situated, affects commerce among the States or with foreign nations." *Fry v. United States*, 421 U.S. 542, 547 (1975); *Wickard v. Filburn*, 317 U.S. 111, 127-28 (1942). The "activity" here—written agreements between parties of different States for the provision of continuing services that involve materials from other States—readily meets that test.

A. The issue before this Court arises, therefore, only because the Alabama Supreme Court held that Congress did *not* utilize the full extent of its power under the Commerce Clause, thus leaving room for state policies hostile to arbitration within the field. But neither the court below, nor any other court, is able to support that view by reference to the language—or the policies (*see* pages 17-20 *infra*)—of the Act. To the contrary, the language points in just the opposite direction. The field to which Section 2 applies is marked out as any "transaction involving commerce," and Section 1 defines "commerce" to mean "commerce among the several States." The words of that definition, of course, are exactly the same as the words used to define the power given to Congress under Article

I: "to regulate commerce among the several States." Thus, in the absence of other language compelling a narrower construction, the most natural reading of Sections 1 and 2, taken together, is that Section 2 applies throughout the field ("commerce among the several States") over which Congress has power under Article I.

The remainder of Section 2, however, is bereft of any narrowing language. In particular, although Congress could have defined the coverage of the Act by reference to transactions "in" commerce, it chose not to do so, but extended the Act to transactions "involving" commerce. That term, on its face, is broader and more inclusive. *See, e.g., United States v. Luskey*, 262 U.S. 62 (1923); *United States v. James*, 834 F.2d 92, 93 (4th Cir. 1987); *Board of Trade v. SEC*, 677 F.2d 1137, 1146-48 & n.17 (7th Cir.), *vacated as moot*, 459 U.S. 1026 (1982). Indeed, as a matter of common usage, the word "involving" is readily employed to indicate that one matter (here, the transaction) has an effect on, or is related to, a second matter (here, interstate commerce). *See The American Heritage Dictionary of the English Language* 950 (3d ed. 1992) (defining "involve" to mean, *inter alia*, "[t]o influence or affect"). Transactions that affect, or relate to, commerce are within the constitutional power of Congress to regulate. *See* pages 12-13 *supra*.

This understanding of the word "involving" is, in turn, reflected in the discussion of Section 2 in the relevant House Report, on which this Court has previously relied in construing the Act. *See Prima Paint*, 388 U.S. at 401 n.7 (discussed *infra* at page 21). That Report first noted that the remedy provided for in Section 2 is "founded . . . upon the Federal control over interstate commerce." Having established that basis for the Act, it then specifically declared that "[t]he control over interstate commerce reaches not only the actual physical interstate shipment of goods but also *contracts relating to interstate commerce*." H.R. Rep. No. 96 at 1 (emphasis added). *See also* 65 Cong. Rec. 1931 (1924) (Statement

of Rep. Graham) (Act "only affects contracts relating to interstate subjects and contracts in admiralty").[6] And, this Court has made use of the word "involving" to describe the extent of congressional power under the Commerce Clause, pointing out that Congress enacted Section 2 on the basis of that power and observing that the "reach [of the Commerce Clause] would be limited to transactions involving interstate commerce." *Southland Corp.*, 465 U.S. at 14.

The only other words potentially limiting the scope of Section 2 are the words "contract evidencing," which precede the phrase "a transaction involving commerce." But those words, likewise, reveal no intent to exercise the commerce power sparingly. Taken at face value, the language says nothing more than that the contract must be evidence of the *transaction*, not of the "commerce" to which it applies. Thus, so long as the transaction actually "involv[es]" interstate commerce, and so long as the contract "evidenc[es]" the transaction, Section 2 makes the agreement to arbitrate enforceable regardless of whether the parties openly make reference to the interstate elements in their contract.

If there were any question about this reading, a review of the history of the phrase "contract evidencing" confirms that it was not meant to pare back exercise of the commerce power. The phrase was absent from the earlier version of the bill, which applied broadly to "a written provision in any contract or maritime transaction or transaction involving commerce." S. 4214, 67th Cong., 4th Sess. (1922); S. 1005, 68th Cong., 1st Sess. (1923);

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[6] Congress has used the term "affecting commerce" as a way of declaring its intent to exercise its full commerce power, *see Gulf Oil Corp. v. Copp Paving*, 419 U.S. 186 (1974), and the term "involving commerce" is sufficiently close in meaning to signal the same intent. Had Congress wished to indicate that it was invoking less than all of its power, in fact, it is natural to suppose that it would have used the term "in" instead. *See id.* at 194-95.

H.R. 646, 68th Cong., 1st Sess. (1924).[7] That language ("any contract"), if read literally, would have made *all* arbitration provisions enforceable, and, as a consequence, raised the most serious questions about the source of congressional authority. The changed language effectively avoided those questions, confining the statute to those fields within Congress' acknowledged control.[8] *See Southland Corp.*, 465 U.S. at 14-15 (describing the "involving commerce" requirement as a "*necessary* qualification on a statute intended to apply in state and federal courts") (emphasis added). But, while Congress did what was necessary to stay within its allotted powers, there is no reason to think that Congress—legislating with the extent of its own powers in mind—went even further and left some (undefined) portion of its power unexercised.[9] Rather, Congress appears to have done just what the language of the Act suggests: tailored the scope of the Act to the scope of its power under the Commerce Clause, no more and no less.

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[7] The language of Section 2 was modeled after a New York law, which provided that "[a] provision in a written contract to settle by arbitration a controversy thereafter arising between the parties to the contract . . . shall be valid, enforcible [sic] and irrevocable, save upon such grounds as exist at law or equity for the revocation of any contract." Act of April 19, 1920, ch. 275, 1920 N.Y. Laws 803.

[8] The Fourth Circuit has thus surmised that "[t]his was evidently done because it was realized that Congress had no power to legislate with respect to the validity of contracts generally but only as to the validity of those which related to matters subject to its control." *Agostini Bros. Bldg. Corp. v. United States*, 142 F.2d 854, 856 (4th Cir. 1944).

[9] We note that Congress did not change the introductory language of the bill, which states that the bill is "[t]o make valid and enforceable written provisions or agreements for arbitration of disputes arising out of contracts, maritime transactions, or commerce among the States or Territories or with foreign nations." Pub. L. No. 68-401, 43 Stat. 883 (1925). If that language were given effect with regard to Section 2, of course, it would only serve to extend the coverage of the Act beyond the scope of the maritime and commerce powers, not restrict it to something less.

B. This reading of Section 2 also fits closely with the policies embodied in the Act as a whole. It is well-established that, "[i]n enacting § 2 of the federal Act, Congress declared a national policy favoring arbitration and withdrew the power of the states to require a judicial forum for the resolution of claims which the contracting parties agreed to resolve by arbitration." *Southland Corp.*, 465 U.S. at 10; *Perry*, 482 U.S. at 489. This Court has emphasized that, in deciding whether particular federal statutory claims are appropriate for arbitration, " 'questions of arbitrability must be addressed with a healthy regard for the federal policy favoring arbitration.' " *Gilmer*, 111 S. Ct. at 1652 (quoting *Moses H. Cone*, 460 U.S. at 24).[10] And it has declared that this "healthy regard" for federal policy must be taken into account in resolving other issues involving arbitration as well: "[t]he Arbitration Act establishes that, as a matter of federal law, *any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration*, whether the problem at hand is the construction of the contract language itself or an allegation of waiver, delay, or a like defense to arbitrability." *Moses H. Cone*, 460 U.S. at 24-25 (emphasis added).

These same principles should naturally be applied to construction of the Act itself. Just as the "federal policy favoring arbitration" places a special burden on litigants challenging arbitration of claims under federal statutes—requiring them to show that the federal policy is somehow inapplicable to those claims (*see, e.g., Gilmer*, 111 S. Ct. at 1652; *Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220, 227 (1987))—it should place a similar burden on litigants seeking to avoid arbitration of disputes within the reach of Congress' power under the Commerce

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[10] As the Court stated in *Gilmer*, "[h]aving made the bargain to arbitrate, the party should be held to it unless Congress itself has evinced an intention to preclude a waiver of judicial remedies for the statutory rights at issue." 111 S. Ct. at 1652 (quoting *Mitsubishi Motors*, 473 U.S. at 628).

Clause. In the one case as the other, it is reasonable to presume that, absent other indications, Congress fully intended for its policy to apply. Although this presumption naturally would yield to contrary plain language, there is, as we have discussed, no language in the Act indicating an intent to dispense with federal policy. To the contrary, this Court has observed (with respect to arbitration of statutory claims) that "the [Federal Arbitration] Act itself provides no basis for disfavoring agreements to arbitrate statutory claims by skewing the otherwise hospitable inquiry into arbitrability." *Mitsubishi Motors,* 473 U.S. at 627. By the same token, the Act gives no basis for thinking that Congress meant to limit its application to some indeterminate portion of transactions over which it has constitutional power.

It is difficult, in fact, to imagine any reason why Congress would deliberately base this legislation upon its broad power over commerce and yet exercise only a fraction of that power. There can be no serious concern that the Arbitration Act would so expand federal law as to inundate the federal courts with burdensome litigation: the Act does not itself provide a basis for jurisdiction in the federal courts (*see Moses H. Cone,* 460 U.S. at 25 n.32) and, in any event, the Act contains only a few, clear commands designed to *reduce* litigation by removing the substance of disputes from the courts. Nor is there evidence that Congress affirmatively recognized and wished to defer in some measure to state policies directly contrary to the Act's policy favoring fulfillment of promises to arbitrate. Accordingly, to decide that Congress used only part of its power, this Court would ultimately have to conclude that, regardless of the effect on commerce, Congress intentionally left room for contracting parties to disavow agreements to arbitrate and for States to apply discriminatory laws hostile to arbitration. But that conclusion would run head on into the basic purpose of the Act: to assure that arbitration agreements are given

the same respect as all other contracts. Whereas Congress was unquestionably willing for States to apply *neutral* laws to arbitration agreements—at least with respect to certain issues—it plainly was not willing to have States apply *discriminatory* laws to those agreements.

It is also highly doubtful that Congress would have defined the field in a manner that promotes ancillary litigation about the enforceability of arbitration agreements The Act was passed against a background of "agitation against the costliness and delays of litigation," *Dean Witter Reynolds,* 470 U.S. at 220 (quoting H.R. Rep. No. 96 at 2), and Congress expected that "[t]hese matters can be largely eliminated by agreements for arbitration, if arbitration agreements are made valid and enforceable." *Id.* The benefits of arbitration would be substantially diminished, however, if disputes over the nexus with interstate commerce (or, even worse, over the parties' "contemplation" of interstate commerce) had to be resolved to determine whether agreements to arbitrate are binding in the first place. Although some litigation is presumably unavoidable under any standard, it seems safe to say that litigation will be the least pervasive with respect to whether the contract falls within the field that Congress has power to regulate under the Commerce Clause. Written agreements involving the sale of goods and services will typically be within that field.

A reduction in the number of ancillary disputes will also promote the goal of certainty in commercial dealings. Under federal law, businesses engaged in a transaction involving interstate commerce should be able to rely on an agreement to arbitrate disputes between the contracting parties.[11] But if courts must examine the facts of each

[11] One witness testified that the provisions of the bill sought, among other things, "to reduce the price of commodities to the consumer; . . . on the theory that a merchant in figuring his cost adds to his price a certain amount representing the risk of rejection, claims, fault-finding, etc., even including litigation. If inexpensive but dependable arbitration were possible instead of

transaction to determine whether it fits within some constricted definition of "involving commerce," it frequently will be difficult for businesses to know, at the time that they negotiate contracts, whether agreements to arbitrate are binding or not. Whatever the outcome of litigation over this question, the uncertainty itself is inconsistent with Congress' goal of making arbitration agreements valid and enforceable as a matter of federal law. 9 U.S.C. § 2.

C. Prior decisions of this Court also suggest that Section 2 was intended to have broad reach. The most recent, and clearest, statement of that view was contained in *Perry*, where the Court held that the Act preempted state law barring arbitration of designated claims. *See* 482 U.S. at 491. There, the Court first distinguished provisions of the 1934 Securities Act and related regulations—which it previously had held not to preempt the same state law (*See Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Ware*, 414 U.S. 117 (1973))—on the ground that nothing in those materials had "specifie[d] arbitration as the favored means of resolving employer-employee disputes." 482 U.S. at 490 (quoting *Ware*, 414 U.S. at 135). The Court then went on to state that the preemptive effect of the Federal Arbitration Act was far more extensive, expressly describing it as "a statute that embodies Congress' intent to provide for the enforcement of arbitration agreements *within the full reach of the Commerce Clause.*" *Id.* (emphasis added).

This language reflects an understanding contained in earlier cases as well. Thus, although the Court, in *Bernhardt v. Polygraphic Co. of America*, 350 U.S. 198

costly, time-consuming, and troublesome litigation, the risk would be correspondingly smaller and the price made to conform therewith." Hearing on S. 4213 and S. 4214 Before a Subcomm. of the Comm. on the Judiciary, 67th Cong., 4th Sess. 3 (1923) (Statement of Charles L. Bernheimer, Chairman of the Arbitration Comm. of the N.Y. State Chamber of Commerce).

(1956), held that a particular employment contract did not evidence a transaction involving commerce, it applied a test that reflects the full extent of Congress' power over interstate commerce: it thus declined to apply the Act only after finding "no showing that [the employee] while performing his duties under the employment contract was working 'in' commerce, was producing goods for commerce, or was engaging in *activity that affected commerce*, within the meaning of our decisions." *Id.* at 200-01 (emphasis added).[12] Similarly, a decade later, in *Prima Paint Corp.*, 388 U.S. 395, the Court expressly rejected an argument that Congress had intended Section 2 to apply narrowly only to "contracts between merchants for the interstate shipment of goods," *id.* at 401 n.7, finding no basis for that reading in either the language or history of the Act. The Court found specific support for broader application of the Act in language from the House Report, noted earlier at pages 14-15, which stated that the commerce power exercised by Congress extended to " '*contracts relating to interstate commerce.*' " *Id.* (quoting H.R. Rep. No. 96 at 1 (emphasis added).

The federal courts of appeals, to the extent that they have addressed the issue, have also given the Act broad sweep. *See, e.g., Snyder v. Smith*, 736 F.2d 409, 417-18 (7th Cir.), *cert. denied*, 469 U.S. 1037 (1984); *Societe Generale de Surveillance, S.A. v. Raytheon European Management & Sys. Co.*, 643 F.2d 863, 867 (1st Cir. 1981); *Foster v. Turley*, 808 F.2d 38 (10th Cir. 1986); *Del E. Webb Constr. v. Richardson Hosp. Auth.*, 823 F.2d

[12] By holding that the employment agreement in *Bernhardt* did not "involve commerce"—a somewhat surprising conclusion, given the test that the Court applied—the Court was able to put aside the constitutional question whether, after *Erie R. Co. v. Tompkins*, 304 U.S. 64 (1938), Congress could prescribe substantive rules of decision for diversity cases in federal court. This Court disposed of that question in *Prima Paint*, holding that Congress could do so by exercising its powers over interstate commerce and admiralty. 388 U.S. at 405.

145, 147 (5th Cir. 1987). *See also Woermann Constr. Co. v. Southwestern Bell Tel. Co.*, 846 S.W.2d 790, 792 (Mo. Ct. App. 1993). In a leading decision more than 30 years ago, the Second Circuit—having recounted the history of judicial hostility toward enforcement of arbitration agreements—reasoned that "the Congress took pains to utilize as much of its power as it could and by doing so it sought to reduce to a minimum the danger of judicial rejection on constitutional grounds." *Robert Lawrence Co. v. Devonshire Fabrics, Inc.*, 271 F.2d 402, 407 (2d Cir. 1959), *cert. granted*, 362 U.S. 909, *cert. dismissed*, 364 U.S. 801 (1960). More recently, the Tenth Circuit, noting the federal policy favoring arbitration, concluded that "[t]he requirement that the underlying transaction involve commerce is to be broadly construed *so as to be coextensive with congressional power to regulate under the Commerce Clause.*" *Foster v. Turley*, 808 F.2d at 40 (emphasis added). Similarly, the Fifth Circuit has held that Section 2 applies to any contracts that "*relate* to interstate commerce, a standard that implements the strong federal policy favoring arbitration." *Del E. Webb Constr. v. Richardson Hosp. Auth.*, 823 F.2d at 148. And the First Circuit has declared that "the term 'commerce' in this provision of the Act refers to interstate or foreign commerce and is to be broadly construed." *Societe Generale*, 643 F.2d at 867. *See also Mesa Operating Ltd. Partnership v. Louisiana Intrastate Gas Corp.*, 797 F.2d 238, 243 (5th Cir. 1986) ("Commerce" under the Act includes all contracts relating to interstate commerce); *American Airlines, Inc. v. Louisville and Jefferson County Air Bd.*, 269 F.2d 811 (6th Cir. 1959) (Act was enacted pursuant to Congress' plenary power over interstate commerce); *First Investors Corp. v. American Capital Financial Servs., Inc.*, 823 F.2d 307 (9th Cir. 1987) (Act governs agreements "affecting" interstate commerce).

These decisions, at bottom, all recognize what is apparent from the Act itself: that Congress wanted to make

arbitration agreements enforceable across a broad spectrum of commercial arrangements. The Act does not mandate that parties enter into an agreement to arbitrate their disputes. But, once they have done so, and have done so with respect to a transaction within Congress' power to regulate, then that agreement is to be enforced—to the same extent as any other agreement—as a matter of federal law.

II. SECTION 2 CANNOT BE READ, IN ANY EVENT, TO REQUIRE THAT THE PARTIES CONTEMPLATE SUBSTANTIAL INTERSTATE ACTIVITY

Even if Section 2 were read to exercise less than all of the power granted to Congress under the Commerce Clause, it could not reasonably be read to apply only to situations in which, at the time that the parties entered into the agreement to arbitrate, they "contemplated substantial interstate activity." That test—turning on the parties' state of mind with respect to interstate commerce—finds no basis whatsoever in the Act.

The subjective test, first announced by Judge Lumbard in a concurring opinion some thirty years ago, provides that the decisive inquiry for courts applying Section 2 is simply "whether, at the time [the parties] entered into [the contract] and accepted the arbitration clause, they *contemplated* substantial interstate activity." *Metro Indus.*, 287 F.2d at 387. The various courts following the Lumbard test thus make the scope of federal law turn "not on what in fact happened, but on what was in the contemplation of the parties as manifested in their written agreement." *Id. See, e.g., Burke County Pub. School Bd. of Educ. v. Shaver Partnership*, 279 S.E.2d 816 (N.C. 1981); *Pathman Constr. Co. v. Knox County Hosp. Ass'n*, 326 N.E.2d 844 (Ind. Ct. App. 1975); *R.J. Palmer Constr. Co. v. Wichita Band Instrument Co.*, 642 P.2d 127 (Kan. Ct. App. 1982); *Loche v. Dean Witter Reynolds, Inc.*, 526 N.E.2d 1296 (Mass. App. Ct. 1988); *Lacheney v. Profitkey Int'l, Inc.*, 818 F. Supp. 922 (E.D. Va. 1993). As

might be expected, the application of this test frequently has the effect of diminishing the reach of federal law: in this case, for example, the Alabama Supreme Court did not question that the transaction *in fact* involved interstate activity, but it found the activity insufficient to support an inference that the parties contemplated it at the time of the contract. It thus felt free to apply state, not federal, law.

This view simply cannot be squared with the terms of the Act. The term "transaction involving commerce" calls for an inquiry into the transaction itself, not the expectations of the parties, and the broad definition of "commerce" in Section 1 ("commerce among the several States") provides a wholly objective standard for that inquiry. And, as we have noted (*see* page 15 *supra*), the requirement that the contract "evidenc[e]" the transaction involving commerce—added to prevent application of the Act beyond the extent of Congress' powers—means only that the contract must be evidence of the transaction, not that it reflect the particular interstate elements. Indeed, it would be almost inexplicable for Congress to have wanted the jurisdiction of the Act to depend in every case upon what the parties' *subjectively* understood about the extent of interstate commerce involved.[13]

The opinion of Judge Lumbard, likewise, provides no basis for thinking that Congress had a subjective test in mind. Indeed, while Judge Lumbard discussed the language and history of the Act at some length, he ultimately pulled the "contemplation-of-the-parties" test more or less out of thin air. The bulk of his opinion, in fact, is devoted to establishing a proposition that is, in the main,

[13] It is well accepted, for example, that defendants need not be aware of the jurisdictional elements contained in federal criminal statutes. *See United States v. Yermian*, 468 U.S. 63, 68-69 (1984) (quoting *United States v. Feola*, 420 U.S. 671, 676-77 (1975) ("the existence of the fact that confers federal jurisdiction need not be one in the mind of the actor at the time he perpetrates the act made criminal by the federal statute")).

unobjectionable: that "the purpose of the act was to assure those who desired arbitration and whose contracts *related to interstate commerce* that their expectations would not be undermined by federal judges, or . . . by state courts or legislatures." 287 F.2d at 387 (emphasis added). But, having reached that conclusion, Judge Lumbard announced, in the very next sentence, that the "significant question, therefore," was whether the parties "*contemplated* substantial interstate activity." The word "therefore" notwithstanding, however, the conclusion does not properly follow from the premise.[14] If the parties "desire[] arbitration," and the transaction provided for in their contract in fact "relate[s] to interstate commerce," then nothing more is needed to bring their agreement within the boundaries of the Act, regardless of what they do or do not contemplate about the interstate elements.[15]

The "contemplation-of-the-parties" test, in the end, mixes together two necessary, but ultimately distinct, elements under Section 2: first, an agreement to arbitrate; and, second, a nexus to interstate commerce. The first element requires a subjective inquiry into the "contemplation" of the parties to determine whether a necessary precondition of Section 2 has been met: that is, whether the

[14] Not only does the reference to the parties' "contemplat[ion]" appear from nowhere, but the reference to "substantial" interstate activity does as well. The vagueness of that term—and the prospect of litigation over its application in individual cases—is further reason for doubting that Congress intended to tie enforceability of arbitration agreements to this sort of inquiry.

[15] There is no reason to believe that parties to a contract openly agree to arbitration agreements, while secretly believing that the contract does not involve interstate commerce and that the agreement is thus unenforceable under state law. Nor is there reason to believe that, in a transaction actually involving interstate commerce, Congress would want that strategy to be rewarded. Unless that unexpressed belief would be grounds for avoiding the obligations by any contract, it is not grounds for refusing to comply with an agreement to arbitrate. *See* page 27 *infra*.

parties have entered into a voluntary agreement to arbitrate their disputes. The second element calls for an objective inquiry to determine whether the transaction is within the field over which Congress has legislated and within reach of the powers allotted to Congress under the Constitution. But it completely distorts the Act to combine these independent requirements (one subjective and one objective) into a third (mixed) requirement: that the parties must subjectively "contemplate" the objective elements necessary to bring the transaction within the terms of the statute and the Constitution. Once it has been determined that the parties have agreed to arbitrate their disputes, the inquiry into their intent is properly at an end; the sole remaining inquiry is whether Congress, having exercised its power over interstate commerce, has made that agreement enforceable.[16]

To explain its adoption of the "contemplation-of-the-parties" test, the Alabama Supreme Court has stated openly that the test "better promotes [its] strong public policy against the use of predispute arbitration agreements." *Lopez v. Home Buyers Warranty Corp.*, 628 So.2d 361, 363 n.2 (Ala. 1993), *reh'g denied*, 1993 Ala. LEXIS 1512 (Sept. 24, 1993), *petition for cert. filed*, 62 U.S.L.W. 3430 (Dec. 22, 1993) (No. 93-995).[17] But, to state the

[16] Given that contracts (like the one in this case) are often transferred to other parties, the test would also be extraordinarily difficult to apply. A party assuming a contract from persons meeting the subjective test—*i.e.*, persons who did contemplate the interstate activities—should not be able to avoid arbitration by arguing that he did not have the same state of mind. But it would be highly inconvenient, at best, to inquire into the understanding of the original parties, wherever they may be, before it can be determined whether the arbitration agreement (voluntarily assumed as part of the contract) can be enforced.

[17] The Alabama Supreme Court has recently relied on that same "public policy" in deciding arbitration issues, even with respect to agreements that are concededly within the scope of Section 2. *See Old Republic Ins. Co. v. Lanier*, No. 1921387, 1994 Ala. LEXIS 276 (Ala. Apr. 29, 1994).

obvious, a distrust of arbitration is hardly a good reason to read Section 2 narrowly. As this Court has observed, "we are well past the time when judicial suspicion of the desirability of arbitration and of the competence of arbitral tribunals inhibited the development of arbitration as a means of dispute resolution." *Mitsubishi Motors*, 473 U.S. at 626-27. The Alabama courts and legislature may believe that arbitration agreements are undesirable; but the Act reflects *Congress'* contrary belief that arbitration provides a fair and efficient remedy to persons engaged in contractual disputes. *See id.* at 628 (parties agreeing to arbitrate do not forfeit substantive rights; they only "submit[] to their resolution in an arbitral, rather than a judicial, forum"). And it is clear that, for contracts within the terms of the Act, Congress intended its view of arbitration to prevail.

The federal policy favoring arbitration does not mean, of course, that every arbitration agreement involving interstate commerce is valid and binding. This Court has recognized that agreements to arbitrate may "result[] from the sort of fraud or overwhelming economic power that would prove grounds 'for the revocation of any contract.'" *Mitsubishi Motors*, 473 U.S. at 627 (quoting 9 U.S.C. § 2); *see Gilmer*, 111 S. Ct. at 1655-56. If that is the case, the agreement need not be enforced. But, as the language of Section 2 makes clear, the grounds on which States may refuse to enforce arbitration agreements must be grounds that apply to other contracts as well: "Thus state law, whether of legislative or judicial origin, is applicable *if* that law arose to govern issues concerning the validity, revocability, and enforceability of contracts generally." *Perry*, 482 U.S. at 492 n.9. On the other hand, "[a] state-law principle that takes its meaning precisely from the fact that a contract to arbitrate is at issue does not comport with this requirement of § 2." *Id.*

The Alabama law involved here—a law expressly barring enforcement of predispute arbitration agreements—is the most notorious possible example of a state-law prin-

ciple that applies to arbitration agreements alone. To avoid preemption of that state law, therefore, the Alabama courts had no choice but to adopt a reading of Section 2 that made federal law wholly inapplicable. But a State may not shelter laws hostile to arbitration by turning that same hostility towards construction of federal arbitration law. Here, parties in different states entered into a contract for a continuing service, and that service involved materials brought from one state to another. By any reasonable standard, those dealings are a "transaction involving commerce," and the parties' agreement to arbitrate disputes arising out of that transaction must be enforced as a matter of federal law.

CONCLUSION

The judgment of the Supreme Court of Alabama should be reversed.

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